S&P Global Ratings

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Summary:

Jim Hogg County Independent School District, Texas; School State Program

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Credit Profile		
US$4.29 mil unltd tx rfdg bnds ser 2021 dtd 10/01/2021 due 02/15/2034		
Long Term Rating	AAA/Stable	New
Underlying Rating for Credit Program	A/Stable	New
Jim Hogg Cnty Indpt Sch Dist PSF/CRS		
Long Term Rating	AAA/Stable	Current
Underlying Rating for Credit Program	A/Stable	Affirmed

Rating Action

S&P Global Ratings assigned its 'AAA' long-term program rating and its 'A' underlying rating to Jim Hogg County Independent School District (ISD), Texas' approximately $4.29 million 2021 general obligation (GO) unlimited-tax school building and refunding bonds. At the same time, we affirmed our 'A' underlying rating on the district's general obligation (GO)-backed debt outstanding. The outlook is stable.

The long-term rating reflects our assessment of the district's qualification for, and the guarantee provided by, the Texas Permanent School Fund (PSF) bond guarantee program. The program provides the security of a permanent fund of assets that the district could use to meet debt service on bonds guaranteed by the program. (For more information on the long-term program rating, please see our full analysis on the Texas PSF, published June 25, 2021, on RatingsDirect.)

The bonds are payable from a continuing direct annual ad valorem tax levied by the district, without legal limit as to rate or amount, on all taxable property within its borders. Proceeds from the 2021 bonds will be used to refund existing debt for savings without extension of maturities. Post-issuance, the district will have approximately $17.8 million in total direct debt outstanding.

Credit overview

Management attributes recent reserve declines to increased instructional costs and overstaffing, alongside some capital spending. Reserves declined from 25% of operating expenditures in fiscal 2017 to 5.5% in fiscal 2020. The district has historically maintained reserves between 12% and 25% of expenditures. For fiscal 2021, a sizable surplus is expected due to cuts that have been implemented. Given this, and mid-year budget-to-actual reports showing this sizable surplus, we expect reserves will remain at least strong over the next two years. The local economy in south Texas remains rural and limited, albeit stable, with exposure to the oil and gas sector and taxpayer concentration. Debt remains moderate, in our view, while pension costs are minimal due to the state's assistance with these costs.

The rating reflects our opinion of the district's:

- Limited local economy primarily focused on agriculture and oil and gas activities;
- Concentrated tax base with a windfarm as its leading taxpayer;
- Low incomes that have declined recently and strong market value per capita;
- Enrollment that declined due to COVID-19 but is expected to return to its historical average;
- Good cash-based reserves that have decreased by roughly 71% since fiscal 2017 due primarily to increasing instructional costs and overstaffing; and
- Moderate debt repaid fairly rapidly and limited pension costs due to the state's contribution on behalf of school districts.

Environmental, social, and governance factors

We have analyzed environmental, social, and governance (ESG) risks relative to the district's economy, financial management, budgetary performance, flexibility, and debt-and-liability profile. We think the local economy's dependence on the oil-and-gas sector exposes the district to higher environmental risks relative to its peer group due to potential changes in federal regulations pertaining to carbon emissions and the transition to renewable energy; both could adversely affect the oil-and-gas industry and, in turn, pressure the local economy. In our opinion, social and governance risks are in line with the sector standard.

Stable Outlook

Downside scenario

We could lower the rating if reserves were to decrease further, despite projections for an increase for fiscal 2021, to levels we no longer consider comparable with those of similar-rated peers, whether due to planned capital spending or ongoing structural imbalance.

Upside scenario

Assuming all other rating factors remain stable or improve, we could raise the rating if reserves increase to and are maintained at a level we consider strong or very strong alongside improvement in the district's economic metrics to levels more comparable with those of higher-rated peers.

Credit Opinion

Local economy based on agriculture and oil-and-gas-sector activity with taxpayer concentration

The district, roughly 150 miles south of San Antonio, is in a rural part of south Texas with a local economy focused on agriculture and oil and gas-related activity. Agricultural production includes hay, cattle, and milk. Oil and gas activity contains a mix of midstream and upstream activity, with the largest oil and gas taxpayers in the district being pipeline companies. The limited local economy and the presence of a windfarm lead to a concentration in the top ten taxpayers. However, the level of concentration has historically been stable, and the presence of midstream oil and gas activity leads to a more stable assessed valuation trend through periods of oil price changes given that their assessed value (AV) is based on the value of the improvements on the land primarily. The single largest taxpayer is a windfarm, but under the arrangement of a 313 agreement, its valuation is largely exempt from the district's maintenance and operations (M&O) tax rate and is only applicable to the interest and sinking (I&S) tax rate until 2024. Overall, we think AV will likely remain relatively stable during the next few fiscal years. We recognize COVID-19 did not hinder tax base growth or change leading taxpayers or employers.

Weakened, but still good, finances after continued fund balance declines related to increasing expenditures

For fiscal 2020, the district posted its third consecutive deficit, reducing reserves from very strong, in our view, at 25% of expenditures in fiscal 2017 to good, in our view, at 5.5% of expenditures in fiscal 2020. Management attributes prior decreases to increasing instructional costs during this period due to overstaffing and mandated teacher raises per state legislation. For fiscal 2021, however, a surplus of roughly $1.8 million is projected due to the implementation of cost-cutting measures including staff reductions in May 2020 and attrition efforts throughout calendar 2020. With this expected surplus, reserves will increase to what we consider very strong at 23% of estimated general fund expenditures. However, if the district needs to hire additional teachers, or needs to spend for capital projects, reserves could remain pressured. Over the next two years, we expect the district's reserves to at least remain in compliance with its informal fund balance minimum which is equal to two months of expenditures, or roughly 17%, or we could lower the rating.

Local revenues have remained relatively stable in recent years and state aid revenue has increased in the years following the passing of House Bill 3, whereby districts had to reduce their M&O levy to provide property tax relief, but in many cases received greater state aid. Property taxes generate 25% of general fund revenue and state aid accounts for 63%. For fiscal 2022, officials adopted a balanced budget, although another surplus is expected given the recent staffing reduction.

A wealth-equalization formula, based on property values and average daily attendance (ADA; property wealth per student), determines state funding for all school districts. Therefore, increases or decreases in ADA (enrollment) can lead to corresponding increases or decreases in the amount of state revenue a district receives. Enrollment totaled 1,150 in 2020, but decreased to 1,139 in 2021 and an estimated 1,056 in the 2022 school year due to COVID-19. Officials indicate that the figure for the 2022 school year is a conservative estimate and that actual enrollment is higher so far during the school year and is likely to end higher toward the end of the year.

As part of legislative changes, beginning in fiscal 2020, the district compressed the O&M tax rate to 97 cents per $100 of AV from $1.04. For fiscal 2021, the O&M rate was 95 cents and the I&S rate was 33 cents.

Standard financial management practices and policies with budget adjustments made for fiscal 2021

Management reviews historical enrollment, staffing, AV, and past financial performance when developing revenue and expenditure assumptions, though increasing instructional costs were a primary cause of the recent structural imbalance in the general fund. Beginning for fiscal 2020, management began incorporating recent House Bill 3 school funding changes. In addition, officials use information from the county appraiser.

Management provides the school board with monthly updates on budget-to-actual results; the board could amend the budget, as needed. With recent audited results showing continuous deficits, we do not think budgetary amendments or updates have been fully effective recently, but changes to staffing during fiscal 2020 should help align revenue and expenditures beginning in fiscal 2021. The district adheres to the Texas Public Funds Investment Act and provides, at least, monthly updates. It also maintains a formal investment-management policy. Management's formal fund-balance policy calls for maintaining a minimum of two months' operating expenditures in available reserves, which it is not meeting currently but will likely meet at fiscal year-ends 2021 or 2022. We understand management does not maintain a long-term financial plan or formal long-term capital plans or debt-management policies.

Moderate debt with fairly rapid amortization and no additional debt plans

The district does not currently have any additional debt plans. It privately placed its series 2019A unlimited-tax school building bonds, its series 2019 unlimited-tax school building bonds, and its series 2019 maintenance tax notes. We do not believe these private placements pose a liquidity risk to the district as the terms do not allow for the immediate acceleration of debt service. Additionally, the district is planning to refund the series 2019A and 2019 unlimited-tax bonds with the current series 2021 bonds. The series 2019 maintenance tax notes are expected to be refunded with an upcoming private placement that will close in October. With fairly rapid amortization, debt ratios could improve over the near-to-medium term if no additional debt is issued and the population and AV remain relatively stable.

Pension and other postemployment benefit (OPEB) highlights

We do not view pension and OPEB liabilities as an immediate credit pressure for the district because required contributions currently make up a small portion of total governmental expenditures; however, we expect required contributions to increase during the next few fiscal years but not to levels that should greatly affect operations.

As a Governmental Accounting Standards Board nonemployer contributing entity, the state contributes a sizable share of employer contributions and carries responsibility for the proportionate share of unfunded liabilities.

As of Aug. 31, 2020, the district participated in:

- Texas Teachers' Retirement System (TRS), which was 75.5% funded, with a proportionate share of the net pension liability equal to $3.9 million; and
- Texas Public School Retired Employees' Group Insurance program (TRS-Care), providing health insurance to TRS members, which was 4.9% funded, with a proportionate share of the net OPEB liability at $4.3 million.

Since TRS contributions are on a statutory basis and typically lower than actuarially determined contributions, fiscal 2020 TRS contributions were materially lower than our static and minimum funding-progress metrics; however, legislative changes increasing contribution rates will likely improve both funding metrics. TRS' 29-year, level-dollar, open-amortization schedule will likely result in slow funding progress. Furthermore, the 7.25% discount could lead to some contribution volatility. (For more information on TRS and Texas' pension landscape, see the article, titled "Pension Spotlight: Texas," published Feb. 25, 2020.)

Jim Hogg Independent School District, TX -- Key Credit Metrics

	Characterization	Most recent	Historical information		
			2020	2019	2018
Economic indicators					
Population			5,211	5,156	5,114
Median household EBI % of U.S.	Low		54	64	66
Per capita EBI % of U.S.	Low		57	59	62

Jim Hogg Independent School District, TX -- Key Credit Metrics (cont.)					
	Characterization	Most recent	Historical information		
			2020	2019	2018
Market value ($000)		410,547	417,612	395,418	406,336
Market value per capita ($)	Strong	78,785	80,140	76,691	79,456
Top 10 taxpayers % of taxable value	Concentrated	44.6	46.0	44.6	44.8
Financial indicators					
Total available reserves ($000)			815	1,688	1,892
Available reserves % of operating expenditures	Good		5.5	10.1	14.4
Total government cash % of governmental fund expenditures			7.8	1.7	3.9
Operating fund result % of expenditures			(5.7)	(0.5)	(8.3)
Financial Management Assessment	Standard				
Enrollment		1,056	1,150	1,154	1,146
Debt and long-term liabilities					
Overall net debt % of market value	Moderate	5.0	5.4	5.9	3.5
Overall net debt per capita ($)	Moderate	3,956	4,301	4,496	2,757
Debt service % of governmental fund noncapital expenditures	Moderate		10.2	5.2	5.2
Direct debt 10-year amortization (%)	Fairly Rapid	73	68	62	54
Required pension contribution % of governmental fund expenditures			1.5	1.1	1.3
OPEB actual contribution % of governmental fund expenditures			0.4	0.3	0.4
Minimum funding progress, largest pension plan (%)			68.7	63.4	71.6

EBI--Effective buying income. OPEB--Other postemployment benefits.

Related Research

- Through The ESG Lens 2.0: A Deeper Dive Into U.S. Public Finance Credit Factors, April 28, 2020